The Loyalty Spectrum...The Four Different Types of Loyalty

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I - Is There More Than One Path to Nirvana?

Many of us make our living working with, developing, strategizing and executing “loyalty programs” that are, hopefully intended to increase revenue and keep customers coming back over time. And generally we all play in the same loyalty ballpark, with the implicit deal with the customer being:

“You keep coming back to our business and we’ll reward you with value that you can exchange for stuff, and we’ll also give you some good deals that you can use right now.”

That’s pretty much it. And the same types of programs are applied to airlines, credit cards, hospitality, food service and retail. We all know that there are some limitations to this model—a saturated market, little differentiation within categories, high cost, etc.—but when they’re executed really well for a long period of time they can achieve their objectives and drive profits.

But what if there were other ways to get to the same place? What if there were different ways to view loyalty as it relates to business? What if we’re focusing on the wrong thing at the wrong time?

We all know the parable of the elephant described by blind men who are touching different parts of the elephant. Each has a perfectly valid description of one piece of the elephant but none is aware of the others, nor of the bigger picture that actually makes an elephant an elephant. I’m thinking that loyalty might have a strong connection to this parable. We’re all describing (in infinite, complex, and agonizing detail) one type of loyalty and one type of loyalty program, but are there other types of loyalty that aren’t being considered that might be relevant to a conversation on changing customer behavior?

Here’s a hypothesis: There is a spectrum of types of loyalty that consumers apply toward the businesses and products that they use depending on their perception of and attitude toward the brand.

This spectrum of loyalty is driven by two key factors:

- The level of interest/engagement that the consumer has in the brand, service or category over other brands, services or categories
- The perceived differentiable value that the product or service delivers for a customer.

It seems fairly obvious that the degree to which a customer is loyal to a business would be driven by how interested they are in a specific business or category along with the value that they believe the product or service provides them. And if that’s the case then there must be different ways that a business can drive positive customer response based on those two factors.
II – The Four Types of Loyalty

I’ve identified four types of loyalty— inertial, functional, transactional and emotional— based on these two factors. Each of the four reflects a different level of differentiable value and interest (as shown below):

- **Inertial** (Low Differentiable Value/Low Interest) – Inertial loyalty is repetitive customer behavior driven by the customer’s tendency to not change companies once they’re involved with them. A great example is retail bank customers who really don’t care about or even don’t like their bank, but they are so connected through direct deposits, online bill pay etc. that the hassle of closing all that stuff and re-opening it somewhere else overcomes any desire to move. It’s entirely possible to establish and maintain long-term relationships in a commodity business with customers who don’t care about you, if there are other reasons to stay.

- **Functional** (High Differentiable Value/Low Interest) – When my daughter was an infant, we put her on a specific formula that wasn’t nearly as available as other

- **Emotional** (High Differentiable Value/High Interest) –

- **Transactional** (Low Differentiable Value/High Interest) –

It’s important to remember that any business in any of these categories will have fiercely loyal as well as totally indifferent customers. The intent here is to describe the most likely behaviors that can be expected for each of the different types of loyalty.

Here are descriptions of the four types of loyalty:

1) **Inertial** (low differentiable value/low product-service interest) – Inertial loyalty is repetitive customer behavior driven by the customer’s tendency to not change companies once they’re involved with them. A great example is retail bank customers who really don’t care about or even don’t like their bank, but they are so connected through direct deposits, online bill pay etc. that the hassle of closing all that stuff and re-opening it somewhere else overcomes any desire to move. It’s entirely possible to establish and maintain long-term relationships in a commodity business with customers who don’t care about you, if there are other reasons to stay.

2) **Functional** (high differentiable value/low product-service interest) –
brands, a mistake that we regretted early and often. So, whenever we needed formula, we would scour the supermarkets to find that brand and then buy as much as we could find. Once our daughter was done with formula, we celebrated with a nice glass of champagne and never bought the stuff again. This is functional loyalty. A product or brand that fills a specific need for a customer that no other brand or product type can adequately fill. For the period of time that the product is needed, the value of the product is through the roof, and neither price nor incentives have much of a chance of changing the customer’s habits. But once the customer is done, they’re done, and there’s no way to get them back. Unless they have another kid.

3) **Transactional** (low differentiable value/high product-service interest) – This is where most of our programs live—a structure that rewards customers for each specific transaction with the brand or the product. It makes sense because the one place where a retailer or a credit card issuer can be sure that they know who the customer is and what they’re doing is at the moment of transaction, and they can validate their decision to use the brand. It’s easier to keep score with a transactional program since transactions are nearly always measured. It’s also a place where the customer is vitally interested in the brand because they absolutely need to know that the product or service that they are using will do what it’s supposed to do, because the consequences if it doesn’t work are not good.

4) **Emotional** (high differentiable value, high product/service interest) – This is the real deal, an emotional connection between or among individuals or groups. It’s what we talk about when we speak of “brand advocacy.” It’s what we dream of. And it’s really, really hard to achieve in a business/human relationship. All of us can name a few examples of companies that elicit this level of loyalty—e.g. Apple, Nordstrom, USAA, etc.—and each of us has specific merchants and service providers that we’re emotionally connected to (an example for me is my local sushi bar).

Emotional loyalty doesn’t require rewarding transactions, although that might be a component of a company’s overall loyalty plan. It is driven by the perception by the customer that they are the recipients of service or products that are sufficiently valuable to warrant a commitment to that business that’s manifest in emotional behavior, i.e. recommending the company to friends (and near-friends on Facebook), skewing purchase behavior to the preferred business or brand in spite of price, or ignoring nuisances that might lead to product switching in brands that had less emotional equity. But it’s not essential for many, if not most loyalty applications and the businesses that offer them, nor is it even achievable in a lot of situations.

So why is it important to consider the idea of a spectrum of loyalty? Because there are real opportunities to increase program performance and efficiency by understanding
the type of loyalty you want to drive and the levers that drive that kind of loyalty, and as importantly, NOT spending resources to drive behavior that’s unnecessary or too difficult to achieve. Some people in the discipline will argue that a company should have a holistic vision of loyalty to migrate customers from purely inertial behavior up to emotional loyalty, manifest in new customer referrals and brand advocacy. While this may be doable, it’s a really long haul and it takes a significant investment in the customer to get there. It’s not likely that the return on that investment will justify the effort, and in some cases it’s nearly impossible given the vagaries of customer service at different touch points and the nature of the relationship.

III – What Now?

So what does one do if one finds oneself in one of these categories? Apply and adapt the concepts of loyalty to your objectives, your type of business and type of customers. Here are some sample strategies for the different types of loyalty:
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<th>Loyalty Type</th>
<th>Example Business Categories</th>
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| Inertial     | Retail Banking, Gas and Convenience stores, Cable TV providers, Mobile Network Operators | • Deepen relationship with add-on products and services that make it difficult for the customer to switch  
• Minimize risk of customer disruption by delivering consistent product quality, responsive customer service and stable product delivery | • Incentives to deepen relationship  
• Bounce-back coupons,  
• Bundled product incentives |
| Functional   | Specific use products/services (e.g. diapers) | • Cross-sell into line extensions  
• Use promotion to increase purchase frequency  
• Use life-cycle analysis and forecasting to identify prospective repeat sales opportunities | • In/On-pack cross sell coupons,  
• Social media customer endorsement referral incentives  
• Predictive analytics |
| Transactional| Payments (credit/debit/online/mobile), Airlines, QSR | • Drive increased transaction volume  
• Borrow interest from emotional loyalty business categories (e.g. Sports)  
• Develop experiential reward structures for heavy users (e.g. preferred customer activities/events) | • Structured rewards programs with short and medium term incentives  
• Experiential rewards,  
• Targeted/customized messaging  
• Rewards at or near the actual transaction (POS) |
| Emotional    | Cars, Upscale retail, Sports teams (e.g. NASCAR/NFL), Clothing brands | • Focus on the attributes of the business that drive emotional loyalty  
• Use personalized communications to validate the customer’s relationship with the business  
• Use customers as active advocates for the brand | • Exclusive events  
• Personalized communication  
• Affinity groups/fan clubs  
• Referral rewards |
Some businesses are going to have customers that are in different categories, such as a specialty retailer with a small cohort of emotionally loyal customers and a larger group of occasional customers that might fall into the “functional” category. The business question becomes whether it’s economically viable to have different approaches for different customer types, or to focus on one over the other.

Here are a few thoughts to help you optimize a program based on the type of loyalty that you want to use:

1) **Know what works for your business** – If you’re a business that does just fine on inertia, then it may be smarter to invest in ways to increase customer stickiness instead of incenting behavior change. Or, if you sell very high end merchandise delivered through a high touch sales channel, emotional loyalty is what matters and you may want to concentrate on ensuring that the customer experience is consistently high across your system.

2) **Focus on what will work and ignore what won’t** – If you drive business with a transactional loyalty program, work on enhancing the value of the transaction by using information to deliver a more personalized communication, and broaden the opportunity to drive transactions by using technology to deliver incentives before, during and after the transaction.

3) **Have realistic expectations** – Moving from an inertial loyalty offering to the love fest of emotional loyalty is a very long, and expensive haul, and it might not pay for itself. Do the math and make sure that what you want to achieve will actually deliver an acceptable ROI.

To conclude, there are only three things that any program to change customer behavior should do:

1) Profitably increase average spend per transaction
2) Profitably increase frequency of usage/visits
3) Increase per customer profitability in a given period.

That’s it. Nothing else is relevant, so think about what it is that you want your program to accomplish, think about the level of engagement and brand affinity that your customers have with the brand, identify the type of loyal behavior that you need to elicit, and invest accordingly.